



Financial Management Report as of DECEMBER 31, 2009

AT A GLANCE:

General Fund:

• Higher public utility tax and business license fees place 2009 revenue ahead of 2008.

• Sales and utility taxes and development fees slump.

• Even with utility tax rate and business fee structure change, 2009 revenues below budget.
(page 3)

2009 Sales tax revenue down significantly
(page 5)

Development-related fee revenue significantly down (page 3)

Potential no more
(page 2 sidebar)

Have we hit bottom yet?
(pages 7-8)

Inside this issue:

Expenditure Summary	2
General Fund Revenue	3
General Fund Expenditures	4
Sales Tax Revenue	5
Economic Environment	7
Investment Report	8
Reserve Summary	10

Summary of All Operating Funds: *Revenue*

General Government budgets were adjusted downward in June and December 2009 in response to the significant revenue shortfall. Reserves and expenditure reductions were used to offset the shortfall. Further reductions were taken in December after the voted private utility tax rate increase failed, which reduced 2010 budgets.

- **General Fund** actual 2009 revenue ended **3.6 percent higher** than last year, but **significantly lower than originally planned**. The increase in revenue was largely the result of an increase in the tax rate on public utilities in 2009, the change in the business license fee structure, and an increase in internal engineering charges from several large capital projects. The impact of the declining economy resulted in significant reductions in sales tax and planning fee revenues. Budgeted sales and utility tax revenues were adjusted downward in June. A more detailed analysis of General Fund revenue can be found on page 3, and sales tax revenue performance can be found beginning on page 5.
- **Other General Government Funds** actual 2009 revenue ended **1.2 percent lower than** last year. Internal rates were reduced for fleet (recognizing lower fuel prices) and technology (reduced personnel costs and use of fund cash for replacement charges as a budget reduction strategy). Recreation revenue increased primarily due to an accounting change in 2009 that moved all recreation revenue to the Recreation Revolving Fund. Lodging tax revenue and motor vehicle fuel tax revenue are down 23.4 percent and 9 percent respectively compared to last year. Motor vehicle fuel tax is collected on a flat rate per gallon, so increased fuel costs (resulting in less gas purchased) have a negative impact on this revenue. Lower fuel prices have moderated declines in this revenue as the year progressed.
- **Water Sewer Operating Fund** actual 2009 revenue ended **3.7 percent higher than** last year due to higher utility revenue from higher rates, but moderated by a significant decrease in connection charge fee revenue from declining development activity.
- **Surface Water Management Fund** actual 2009 revenue ended **1.6 percent higher than** last year. Rates are paid through property taxes, which are primarily received in April and October.
- **Solid Waste Fund** actual 2009 revenue ended **1 percent higher than** last year.

Resources by Fund	Year-to-Date Actual			Budget			% of Budget	
	12/31/2008	12/31/2009	% Change	2008	2009	% Change	2008	2009
General Gov't Operating:								
General Fund	52,507,908	54,390,709	3.6%	53,895,913	54,549,760	1.2%	97.4%	99.7%
Other General Gov't Operating Funds	17,130,326	16,927,695	-1.2%	16,562,562	16,563,457	0.0%	103.4%	102.2%
Total General Gov't Operating	69,638,234	71,318,404	2.4%	70,458,475	71,113,217	0.9%	98.8%	100.3%
Utilities:								
Water/Sewer Operating Fund	17,841,773	18,502,180	3.7%	17,821,208	19,807,210	11.1%	100.1%	93.4%
Surface Water Management Fund	5,330,988	5,418,523	1.6%	5,274,145	5,350,962	1.5%	101.1%	101.3%
Solid Waste Fund	8,516,909	8,599,186	1.0%	8,365,262	8,612,724	3.0%	101.8%	99.8%
Total Utilities	31,689,670	32,519,889	2.6%	31,460,615	33,770,896	7.3%	100.7%	96.3%
Total All Operating Funds	101,327,904	103,838,293	2.5%	101,919,090	104,884,113	2.9%	99.4%	99.0%

Budgeted and actual revenues exclude resources forward and interfund transfers.



Annexation Approved— P(otential) A(nnexation) A(rea) now just AA

At its December 15 meeting, the Kirkland City Council took action to accept the annexation of the Finn Hill, North Juanita and Kingsgate neighborhoods. Voters in these neighborhoods approved annexation by just short of 60 percent in the November 2009 election.

This largely residential area is approximately seven square miles, extending north of Kirkland to approximately NE 145th Street. It adds about 33,000 people to the city's current population of 48,000. The annexation will make Kirkland the twelfth largest city in Washington and the sixth largest city in King County. The annexation is scheduled to become effective as of June 1, 2011. For information, visit www.ci.kirkland.wa.us/annexation.

Summary of All Operating Funds: *Expenditures*

- **General Fund** actual expenditures ended **4.1 percent higher than** last year primarily due to higher personnel costs and an accounting change that moved all recreation expenditures to the General Fund (see the explanation of the accounting change in the box below).
- **Other Operating Funds** actual expenditures ended **12.6 percent lower than** last year due to the previously mentioned accounting change for Recreation Revolving fund expenditures, timing of vehicle and computer purchases, substantially lower fuel costs (down 37.3 percent) and despite generally higher personnel costs.
- **Water/Sewer Operating Fund** actual expenditures ended **7 percent higher than** last year due to higher water purchase (up 14 percent) and METRO sewer costs (up 12 percent) and despite a significant decline in regional water connection charges (with a corresponding reduction in connection revenue).
- **Surface Water Management Fund** actual expenditures ended **19.9 percent higher than** last year due to higher personnel costs and internal charges.
- **Solid Waste Fund** actual expenditures ended **1.3 percent lower than** last year.

An accounting change for the Recreation Revolving Fund occurred in 2009. The fund is now used to account for all parks and recreation-related revenue. All expenditures related to parks and recreation programs (except for excise taxes on revenue) are consolidated in the General Fund. A periodic interfund transfer is budgeted from the Recreation Revolving Fund to the General Fund. The purpose of the accounting change was to better identify the General Fund subsidy of recreation programs and functions.

Expenditures by Fund	Year-to-Date Actual			Budget			% of Budget	
	12/31/2008	12/31/2009	% Change	2008	2009	% Change	2008	2009
<i>General Gov't Operating:</i>								
General Fund	55,049,504	57,300,199	4.1%	56,149,141	59,175,445	5.4%	98.0%	96.8%
Other General Gov't Operating Funds	15,089,716	13,187,195	-12.6%	15,817,164	15,415,335	-2.5%	95.4%	85.5%
Total General Gov't Operating	70,139,220	70,487,394	0.5%	71,966,305	74,590,780	3.6%	97.5%	94.5%
<i>Utilities:</i>								
Water/Sewer Operating Fund	13,653,019	14,613,569	7.0%	13,718,748	15,555,212	13.4%	99.5%	93.9%
Surface Water Management Fund	2,663,623	3,194,709	19.9%	2,695,982	3,605,721	33.7%	98.8%	88.6%
Solid Waste Fund	8,322,862	8,215,505	-1.3%	8,221,762	8,455,673	2.8%	101.2%	97.2%
Total Utilities	24,639,504	26,023,783	5.6%	24,636,492	27,616,606	12.1%	100.0%	94.2%
Total All Operating Funds	94,778,724	96,511,177	1.8%	96,602,797	102,207,386	5.8%	98.1%	94.4%

Budgeted and actual expenditures exclude working capital, operating reserves, capital reserves, and interfund transfers.

General Fund Revenue

Many significant General Fund revenue sources are economically sensitive, such as sales tax and development-related fees.

- Sales tax** revenue allocated to the General Fund for 2009 ended the year **17.1 percent lower than** 2008. A budget reduction of almost \$2.7 million was made mid-year recognizing the significant decline in actual revenue. A slight improvement in the last quarter brought actual revenue slightly ahead of the reduced budgeted amount. A detailed analysis of sales tax revenue can be found starting on page 5.
- Utility tax** actual revenue collection ended **16.5 percent higher than** last year due to the shift of cable tax revenue from the Facilities Fund and increased tax rate for public utilities (water, sewer, and garbage). Factoring out cable tax, revenue would be up about 6.5 percent. However, revenue fell short of expectations and mid-year budget reductions of almost \$1 million. The reductions were made to reflect reduced actual revenue due to the economic downturn and electricity tax revenue resulting from an unexpected electricity rate decrease. Actual revenue ended up slightly ahead of the adjusted budgeted amount.
- Other taxes** actual revenue ended **6.4 percent higher than** last year primarily due to the shift of admissions tax from the Facilities Fund and despite declining gambling tax revenue.
- The **business licenses (base fee) and franchise fees** actual revenue ended **8.5 percent higher than** last year primarily due to higher franchise fee revenue. The **revenue generating regulatory license** fee ended **92.1 percent higher than** last year due to a significant increase and restructuring of the fee. However, this revenue ended up about **\$660,000 under budget** largely due to the economic recession.
- The severe decline in development activity is reflected in **development-related fee** revenues, which collectively ended **24.8 percent lower than** last year. Compared to 2008, **building permits and plan check revenue** ended collectively **24.1 percent lower**, **planning fees** ended **25.7 percent lower**, and **engineering services** revenue ended **27.3 percent lower**.
- Compared to last year: **Grant** revenue ended **39.2 percent higher** due to funding received for the environmental outreach program; **State shared revenues** ended **22.5 percent higher** due to mitigation revenue received for the loss of sales tax revenue resulting from sourcing rule changes; **Other intergovernmental services** revenue ended **33.7 percent higher** due to a contract providing staffing to the Regional Justice Training Center and higher Fire District #41 contract revenue partially due to additional firefighters added in 2009.
- Internal Charges** ended **34.7 percent higher than** last year primarily due to a significant increase in capital project engineering charges.
- Other charges for services** revenue ended **31.6 percent higher than** last year due to higher probation and prisoner housing/monitoring charges.
- Miscellaneous revenue** ended **25.4 percent higher than** last year due a change to the allocation of interest revenue supporting debt service costs to the General Fund.
- Other financing sources** are significantly **higher than** last year reflecting the use of reserves from other funds to backfill reduced revenues and transfers from the recreation revolving fund from the accounting change described on page 2.

General Fund actual 2009 revenue ended **3.6 percent higher** than last year, but **significantly lower than originally planned**. The increase in revenue was largely the result of an increase in the tax rate on public utilities in 2009, the change in the business license fee structure, and an increase in internal engineering charges from several large capital projects. The impact of the declining economy resulted in significant reductions in sales tax and development fee revenues.

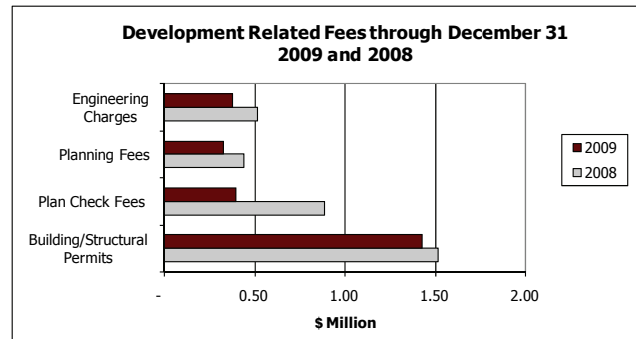
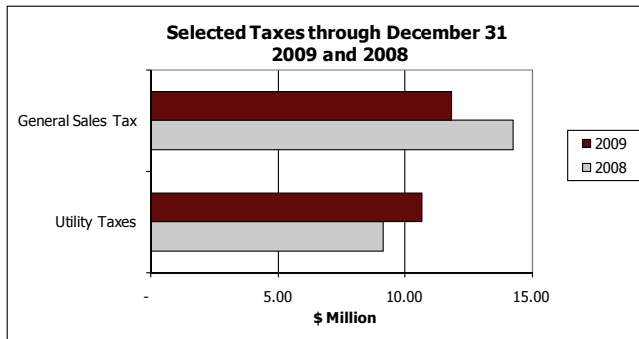
The General Fund is the largest of the General Government Operating funds. It is primarily tax supported and accounts for basic services such as public safety, parks and recreation, and community development.

General Fund Resource Category	Year-to-Date Actual			Budget			% of Budget	
	12/31/2008	12/31/2009	% Change	2008	2009	% Change	2008	2009
Taxes:								
Retail Sales Tax: General	14,261,208	11,824,929	-17.1%	15,756,800	11,564,551	-26.6%	90.5%	102.3%
Retail Sales Tax: Criminal Justice	1,139,408	967,304	-15.1%	1,050,000	1,107,000	5.4%	108.5%	87.4%
Property Tax	9,245,728	9,396,769	1.6%	9,037,710	9,264,941	2.5%	102.3%	101.4%
Utility Taxes	9,161,597	10,672,711	16.5%	8,546,130	10,604,676	24.1%	107.2%	100.6%
Rev Generating Regulatory License	1,008,293	1,936,606	92.1%	990,000	2,599,920	162.6%	101.8%	74.5%
Other Taxes	571,934	608,619	6.4%	664,713	591,779	-11.0%	86.0%	102.8%
Total Taxes	35,388,168	35,406,938	0.1%	36,045,353	35,732,867	-0.9%	98.2%	99.1%
Licenses & Permits:								
Building, Structural & Equipment Permits	1,515,209	1,428,405	-5.7%	2,163,450	1,645,600	-23.9%	70.0%	86.8%
Business Licenses/Franchise Fees	1,547,013	1,678,466	8.5%	1,449,450	1,654,903	14.2%	106.7%	101.4%
Other Licenses & Permits	172,150	185,636	7.8%	193,900	183,500	-5.4%	88.8%	101.2%
Total Licenses & Permits	3,234,372	3,292,507	1.8%	3,806,800	3,484,003	-8.5%	85.0%	94.5%
Intergovernmental:								
Grants	189,139	263,241	39.2%	155,260	218,754	40.9%	121.8%	120.3%
State Shared Revenues & Entitlements	709,705	869,176	22.5%	645,318	908,404	40.8%	110.0%	95.7%
Fire District #41	3,439,879	3,904,235	N/A	3,487,428	3,850,077	N/A	98.6%	101.4%
EMS	793,023	838,397	N/A	793,023	836,938	N/A	100.0%	100.2%
Other Intergovernmental Services	621,709	830,990	33.7%	439,609	654,713	48.9%	141.4%	126.9%
Total Intergovernmental	5,753,455	6,706,039	16.6%	5,520,638	6,468,886	17.2%	104.2%	103.7%
Charges for Services:								
Internal Charges	3,536,860	4,764,301	34.7%	3,511,012	4,905,963	39.7%	100.7%	97.1%
Engineering Services	515,972	375,245	-27.3%	610,000	357,134	-41.5%	84.6%	105.1%
Plan Check Fee	883,729	392,094	-55.6%	900,000	520,000	-42.2%	98.2%	75.4%
Planning Fees	438,350	325,822	-25.7%	1,194,637	247,157	-79.3%	36.7%	131.8%
Recreation*	82,385	-	-100.0%	83,000	-	-100.0%	99.3%	N/A
Other Charges for Services	690,566	908,478	31.6%	688,323	756,426	9.9%	100.3%	120.1%
Total Charges for Services	6,147,862	6,765,940	10.1%	6,986,972	6,786,680	-2.9%	88.0%	99.7%
Fees & Forfeits	1,414,371	1,504,982	6.4%	1,132,000	1,407,595	24.3%	124.9%	106.9%
Miscellaneous	569,680	714,303	25.4%	404,150	669,729	65.7%	141.0%	106.7%
Total Revenues	52,507,908	54,390,709	3.6%	53,895,913	54,549,760	1.2%	97.4%	99.7%
Other Financing Sources:								
Interfund Transfers	1,334,495	4,477,317	N/A	1,441,253	3,899,053	N/A	92.6%	114.8%
Total Other Financing Sources	1,334,495	4,477,317	N/A	1,441,253	3,899,053	N/A	92.6%	114.8%
Total Resources	53,842,403	58,868,026	9.3%	55,337,166	58,448,813	5.6%	97.3%	100.7%

Budgeted and actual revenues exclude resources forward.

*2009 Recreation revenue is accounted for in the Recreation Revolving Fund; See accounting note on page 2.

General Fund Revenue *continued*



General Fund Expenditures

General Fund Department Expenditures	Year-to-Date Actual			Budget			% of Budget	
	12/31/2008	12/31/2009	% Change	2008	2009	% Change	2008	2009
Non-Departmental	1,254,191	1,199,905	-4.3%	1,391,813	1,254,877	-9.8%	90.1%	95.6%
City Council	351,677	343,678	-2.3%	362,034	353,175	-2.4%	97.1%	97.3%
City Manager's Office	3,507,040	3,221,365	-8.1%	3,784,425	3,386,417	-10.5%	92.7%	95.1%
Human Resources	1,026,646	1,009,257	-1.7%	1,122,706	1,081,720	-3.7%	91.4%	93.3%
City Attorney's Office	958,704	1,002,792	4.6%	991,985	993,790	0.2%	96.6%	100.9%
Parks & Community Services	5,851,805	6,959,926	18.9%	6,059,645	7,621,687	25.8%	96.6%	91.3%
Public Works (Engineering)	3,418,006	3,456,369	1.1%	3,578,878	3,686,124	3.0%	95.5%	93.8%
Finance and Administration	3,355,677	3,515,473	4.8%	3,536,915	3,671,314	3.8%	94.9%	95.8%
Planning & Community Development	3,367,756	2,733,663	-18.8%	3,381,197	2,835,702	-16.1%	99.6%	96.4%
Police	15,247,587	16,117,610	5.7%	15,019,785	16,557,994	10.2%	101.5%	97.3%
Fire & Building	16,710,415	17,740,161	6.2%	16,919,758	17,732,645	4.8%	98.8%	100.0%
Total Expenditures	55,049,504	57,300,199	4.1%	56,149,141	59,175,445	5.4%	98.0%	96.8%
Other Financing Uses:								
Interfund Transfers	1,506,971	1,705,441	13.2%	1,594,916	1,705,441	6.9%	94.5%	100.0%
Total Other Financing Uses	1,506,971	1,705,441	13.2%	1,594,916	1,705,441	6.9%	94.5%	100.0%
Total Expenditures & Other Uses	56,556,475	59,005,640	4.3%	57,744,057	60,880,886	5.4%	97.9%	96.9%

Budgeted and actual expenditures exclude working capital, operating reserves, and capital reserves.

Facilities charges (an internal service charge) for General Fund departments were increased as a result of an accounting change. In previous years, cable and admissions tax were allocated directly to the Facilities Fund, which in effect subsidized the rate charged to General Fund departments. Beginning in 2009, these revenues are directly budgeted in the General Fund. The resulting increase to the internal rate charged to the General Fund is covered by the revenue shift.

Comparing to last year:

- Actual 2009 expenditures for **Non-Departmental** ended **4.3 percent lower** primarily due to a one-time refund payment in 2008 for leasehold excise tax over-collected in prior years and despite a significant increase in hydrant maintenance fees paid to the water utility.
- Actual 2009 expenditures for the **City Council** ended **2.3 percent lower** primarily due to a one time citizen survey in 2008 and despite higher facility charges.
- Actual 2009 expenditures for the **City Manager's Office** ended **8.1 percent lower** due to charges incurred in 2008 for setting up a regional dispatch agency, and despite higher internal service charges. Ongoing expenses for the regional dispatch agency are now budgeted in the Police and Fire departments.
- Actual 2009 expenditures for the **City Attorney's Office** ended **4.6 percent higher** due to increased personnel costs, contracted legal costs, and facility charges.
- Actual 2009 expenditures for the **Parks & Community Services Department** ended **18.9 percent higher** primarily due to the recreation revolving accounting change described on page 2, increased personnel costs and facility charges and despite lower operating supply and equipment costs.

2009 General Fund actual expenses ended 4.1 percent higher than 2008 primarily due to higher personnel costs, costs for the new regional dispatch agency, and increased internal service rates as noted to the left.

Actual expenditures ended 3.2 percent under budget primarily due to personnel cost savings and unfinished projects.

(Continued on page 5)

Financial Management Report as of DECEMBER 31, 2009

- Actual 2009 expenditures for the **Finance and Administration Department** ended **4.8 percent higher** due to increased personnel and election costs and facility charges.
- Actual 2009 expenditures for the **Planning and Community Development Department** ended **18.8 percent lower** due to the shift of regional housing funding to another fund, one-time projects that were underway in 2008, and lower personnel costs as a result of reduction in development-related staffing levels.
- Actual 2009 expenditures for the **Police Department** ended **5.7 percent higher** due to charges for the regional dispatch agency and despite no change in personnel costs and lower jail costs. Kirkland dispatch staff were relocated to the new agency as of July 1st. Higher jail costs were a concern in 2008; expenses in 2009 are down about 3.4 percent from last year, but still ended the year \$153,000 over budget, which was offset by under-expenditures in other line items.
- Actual 2009 expenditures for the **Fire & Building Department** ended **6.2 percent higher** due to higher personnel costs (despite reduction to development-related building division staff) and charges for the regional dispatch agency. Fire suppression overtime expenses in 2009 are down 33 percent from last year due to the elimination of one-time funded staffing of Station 24 with overtime and adding staffing to provide more shift coverage. However, overtime still ended the year about \$170,000 over the original budget. Contingency reserves were used to adjust the department budget for the overage.

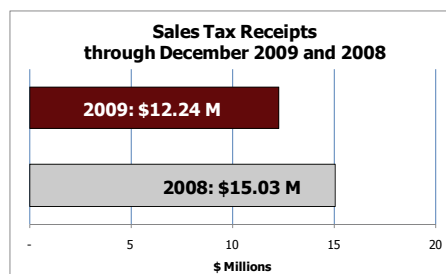


**Green Kirkland Partnership
Volunteers at Cotton Hill Park**

Sales Tax Revenue Analysis Total 2009 actual revenue ended **18.5 percent lower than** last year (almost \$2.8 million). This is a continuation of the generally negative trend that began in the last quarter of 2007 and continued throughout 2008. Primary factors include significant reduction of development activity, as well as weak performance in key retail sectors. Comparative monthly revenue improved at the end of the year, as the comparisons are against months after the recession began at the end of 2008. All business sectors experienced negative performance compared to last year (see table on page 6).

Review by business sectors:

- The **contracting** sector ended **35.9 percent down** compared to last year due to the completion of major projects and significant weakening in development activity due to the current economic recession. A few new large projects are underway, including a new high school and downtown transit center. However, they have not replaced the level of previous activity.
- Auto/gas retail** ended **11.4 percent down** compared to last year due to disappointing performance by key retailers. The last quarter of the year improved substantially, partially due to the "cash for clunkers" incentive program. Several retailers experienced positive sales performance at the end of the year.
- Wholesale** ended **38.2 percent down** compared to last year due to decreased development-related activity and changes to local coding sourcing rules from streamlined sales tax.
- General merchandise/miscellaneous retail** ended **13.5 percent down** compared to last year due to disappointing performance by key retailers, an indication of reduced consumer spending in response to economic conditions. This sector has also been impacted by streamlined sales tax.
- The **services** sector ended **14 percent down** compared to last year largely due to declines in software and car/equipment leasing, as well as impact from the sourcing rule change. The accommodations sector continued its negative performance for the entire year, down 15.1 percent compared to 2008.
- Other retail** ended **13.1 percent down** compared to last year due to generally negative performance in most retail sectors included in this group, especially building materials and electronic equipment. This sector is also impacted by streamlined sales tax sourcing rule changes and the closure of a major retailer.
- Retail eating/drinking** ended **13.1 percent down** compared to last year, continuing the negative trend that started in the second half of 2008. Reduced consumer discretionary spending is evident from the generally negative performance by most businesses in this sector as well as the closure of four restaurants.
- The **miscellaneous** sector ended **17.6 percent down** compared to last year due to slumping finance/insurance and real estate sectors.
- The **communications** sector ended **14.9 percent down** compared to last year due to reduced development-related activity and declining revenue from telecommunications companies.



Streamlined Sales Tax

Washington State implemented new local coding sales tax rules as of July 1, 2008, as a result of joining the national Streamlined Sales Tax Agreement. Negative impact from this change is mitigated by the State of Washington.

Kirkland received about \$290,000 in mitigation payments over the last year. Payments for 2010 have been set at \$131,000 for the year, paid quarterly.

Neighboring Cities

For Bellevue and Redmond, 2009 sales tax revenue declined by 19.1 percent and 6.7 percent respectively compared to 2008.

City of Kirkland Actual Sales Tax Receipts

Business Sector Group	January-December		Dollar Change	Percent Change	Percent of Total	
	2008	2009			2008	2009
Services	1,696,462	1,459,736	(236,726)	-14.0%	11.3%	11.9%
Contracting	2,685,516	1,722,657	(962,859)	-35.9%	17.9%	14.1%
Communications	564,808	480,575	(84,233)	-14.9%	3.8%	3.9%
Auto/Gas Retail	2,990,763	2,650,663	(340,100)	-11.4%	19.9%	21.6%
Gen Merch/Misc Retail	2,230,501	1,930,424	(300,077)	-13.5%	14.8%	15.8%
Retail Eating/Drinking	1,295,765	1,125,423	(170,342)	-13.1%	8.6%	9.2%
Other Retail	1,761,238	1,545,962	(215,276)	-12.2%	11.7%	12.6%
Wholesale	881,824	544,895	(336,929)	-38.2%	5.9%	4.4%
Miscellaneous	924,213	784,591	(139,622)	-15.1%	6.1%	6.4%
Total	15,031,090	12,244,926	(2,786,164)	-18.5%	100.0%	100.0%

Kirkland's sales tax base is comprised of a variety of businesses which are grouped and analyzed by business sector (according to NAICS, or "North American Industry Classification System"). Nine business sector groupings are used to compare 2008 and 2009 year-to-date sales tax receipts in the table to the left.

City of Kirkland Actual Monthly Sales Tax Receipts

Month	Sales Tax Receipts		Dollar Change	Percent Change
	2008	2009		
January	1,227,855	994,146	(233,709)	-19.0%
February	1,586,493	1,224,935	(361,558)	-22.8%
March	1,112,704	954,492	(158,212)	-14.2%
April	1,085,739	867,726	(218,013)	-20.1%
May	1,367,777	1,007,790	(359,987)	-26.3%
June	1,073,093	900,631	(172,462)	-16.1%
July	1,253,751	945,876	(307,875)	-24.6%
August	1,388,993	1,091,599	(297,394)	-21.4%
September	1,335,699	1,107,187	(228,512)	-17.1%
October	1,205,125	1,109,409	(95,716)	-7.9%
November	1,281,997	1,076,996	(205,001)	-16.0%
December	1,111,864	964,139	(147,725)	-13.3%
Total	15,031,090	12,244,926	(2,786,164)	-18.5%

When analyzing monthly sales tax receipts, there are two items of special note: First, most businesses remit their sales tax collections to the Washington State Department of Revenue on a monthly basis. Small businesses only have to remit their sales tax collections either quarterly or annually, which can create anomalies when comparing the same month between two years. Second, for those businesses which remit sales tax monthly, there is a two month lag from the time that sales tax is collected to the time it is distributed to the City. For example, sales tax received by the City in December is for sales activity in October. Monthly sales tax receipts through December 2008 and 2009 are compared in the table to the left.

- Negative monthly comparison trends, with the exception of February 2008, have been occurring since July 2007.
- Sourcing rule changes were adopted as of July 1, 2008 due to streamlined sales tax legislation. Mitigation payments from Washington State help offset the impact of revenue lost due to the changes. Factoring in these payments would change the decline in sales tax revenue between 2009 and 2008 to about 17.1 percent.
- Fourth quarter monthly performance improved slightly from the previous quarter primarily due to two reasons: 1) The economic downturn started in the last quarter of 2008, so the comparative base between the years is reduced, and 2) the federal "cash for clunkers" program helped boost automobile sales (primarily in October).

Kirkland's sales tax base is further broken down by business district (according to geographic area), as well as "unassigned or no district" for small businesses and businesses with no physical presence in Kirkland.

Comparing to last year:

Totem Lake, which accounts for 31 percent of the total sales tax receipts, ended **18.3 percent down** primarily due to slumping automotive/gas

retail sales and generally weak retail and finance/real estate activity. About 65 percent of this business district's revenue comes from the auto/gas retail and general merchandise/miscellaneous retail sectors.

NE 85th Street, which accounts for over 16 percent of the total sales tax receipts, ended **10.4 percent down** primarily due to the general merchandise/miscellaneous retail and automotive/gas retail sectors, which contribute about 86 percent of this business district's revenue.

Downtown, which accounts for over 7 percent of the total sales tax receipts, ended **17.1 percent down** due to the loss of several retailers and poor performance in the retail eating/drinking and accommodations sectors; these sectors provide over 68 percent of this business district's revenue.

Carillon Point/Yarrow Bay, which accounts for over 2 percent of the total sales tax receipts, ended **23.5 percent down** compared to last year primarily due to poor performance from major software companies, retail eating/drinking and the accommodations sectors. Over 76 percent of this business district's revenue comes from business services, retail eating/drinking and hotels.

Houghton & Bridle Trails, which collectively account for over 2 percent of the total sales tax receipts, ended **22.4 percent down** collectively almost entirely due to entertainment/recreation, miscellaneous retail and other retail, which provides over 75 percent of these business districts' revenue.

Juanita, which accounts for about 2 percent of the total sales tax receipts, ended **9.1 percent down** primarily due to the retail eating/drinking sectors. A one-time recovery received in 2008 in this sector skews comparisons between the years. Factoring out the one-time 2008 receipt, this business district would be down about 5 percent. Retail eating/drinking and personal services provide over 45 percent of this business district's revenue.

When reviewing sales tax receipts by business district, it's important to point out that about 40 percent of the revenue received in 2009 is in the "unassigned or no district" category largely due to contracting revenue (which has declined compared to last year), and increasing revenue from Internet, catalog sales and other businesses located outside of the City.

City of Kirkland Sales Tax by Business District

Business District	Jan - Dec Receipts		Dollar Change	Percent Change	Percent of Total	
	2008	2009			2008	2009
Totem Lake	4,638,102	3,790,629	(847,473)	-18.3%	30.9%	31.0%
NE 85th St	2,266,182	2,029,969	(236,213)	-10.4%	15.1%	16.6%
Downtown	1,118,506	927,065	(191,441)	-17.1%	7.4%	7.6%
Carillon Pt/Yarrow Bay	419,800	321,053	(98,747)	-23.5%	2.8%	2.6%
Houghton & Bridle Trails	390,494	302,952	(87,542)	-22.4%	2.6%	2.5%
Juanita	299,503	272,285	(27,218)	-9.1%	2.0%	2.2%
Unassigned or No District:						
Contracting	2,685,045	1,721,878	(963,167)	-35.9%	17.9%	14.1%
Other	3,213,458	2,879,095	(334,363)	-10.4%	23.3%	25.6%
Total	15,031,090	12,244,926	(2,786,164)	-18.5%	100.0%	100.0%

Sales Tax Revenue Outlook Revenue performance for the months of the last quarter of 2009 improved to an average of 12 percent decline compared to the average 20 percent decline experienced over the first three quarters. This helped the year end at 18.5 percent decline, better than previously expected. Hopefully this is a sign that the bottom has been reached and recovery may be in sight. However, December 2009 is still almost 25 percent behind December 2007. Contracting activity has severely slumped with no sign of meaningful change for the near future. The local business climate remains fragile, illustrated by the closure of several businesses over the last year. Overall, 2009 sales tax revenue is almost \$4.3 million behind 2007. If 2010 revenue remains flat (as currently projected) compared to 2009, the current biennium sales tax receipts will decline over \$7 million compared to the previous biennium.

OFFICE VACANCIES:

According to CB Richard Ellis Real Estate Services, the Eastside vacancy rate is 18.3 percent for fourth quarter 2009 compared to 13 percent for fourth quarter 2008. Kirkland's 2009 rate is 30.4 percent, significantly higher than the 2008 rate of 8.6 percent largely due to the completion of the Lakeview Plaza. Google had intended to fully occupy this space, but has put about half of it out for sublease due to the recession.

The Puget Sound region appears to be stabilizing somewhat, with fourth quarter negative absorption of only 263,000 square feet of space compared to more than 2 million square feet returned in the prior 3 quarters. However, the area is still experiencing high vacancy rates and falling rents.

LODGING TAX REVENUE:

Lodging tax 2009 revenue is down 23.4 percent compared to the same period last year.

Economic Environment Update The Puget Sound regional economy appears to be stabilizing, but job growth is still lagging. According to Conway & Pedersen Economics' *Economic Forecaster*, job losses were greater than the rest of the nation because of the strong housing market pushed up construction employment. When the housing market collapsed and the jobs disappeared, the region had farther to fall. Optimism for the region's economic future remains because of the global recovery and the area's close ties to Asia. Boeing's successful first 787 Dreamliner flight and the success of Microsoft's Windows 7 are evidence that Washington State will outperform other states in economic recovery over the next three years according to Washington State's chief economist, Dr. Arun Raha. The rate of job loss has slowed and is expected to peak in the second quarter of 2010. Obstacles to recovery include small business credit availability, depressed construction activity, and low consumer confidence. These same factors will also hamper Kirkland's economic recovery, especially since small businesses comprise a substantial portion of retail activity and the resulting sales tax and business fees. Construction activity not only contributes development fee and sales tax revenues, but also increases the property tax base.

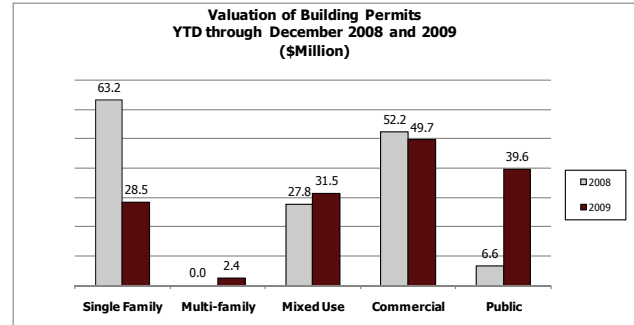
The U.S. **consumer confidence index increased** for the second consecutive month to **52.9** in December from 50.6 in November. This index is closely watched as consumer spending makes up about 2/3 of the nation's economic activity. An index reading of 90 indicates stability and over 100 indicates strong growth.

King County's **unemployment rate is 8.5 percent** in December compared to 5.6 percent in December 2008. This rate is below the Washington State and U.S. rates, which are 9.5 percent and 9.7 percent respectively. Generally, King County falls below these rates.

The **Western Washington chapter of Purchasing Managers survey index fell** again in November (last available) to **56.8**, down by 2.3 points from October. However, this is still a positive indication since an index reading greater than 50 indicates a growing economy and this index has been above 50 for four consecutive months.

(Continued on page 8)

Local **development activity** through December comparing 2009 to 2008 as measured by the valuation of City of Kirkland building permits is illustrated in the chart to the right. Single family activity plummeted, which was offset by the significant increase from two large projects in the public sector as well as some multi-family activity. Commercial/mixed use activity collectively were flat. Overall 2009 permit valuation ended slightly ahead of 2008, although permit revenues fell well short of budgeted levels.



Pending sales of **new and existing single-family homes** on the Eastside were up 78 percent in December 2009 compared to December 2008, the strongest performance in King County. However, median price dropped 5.5 percent (\$520,000 compared to \$550,000).

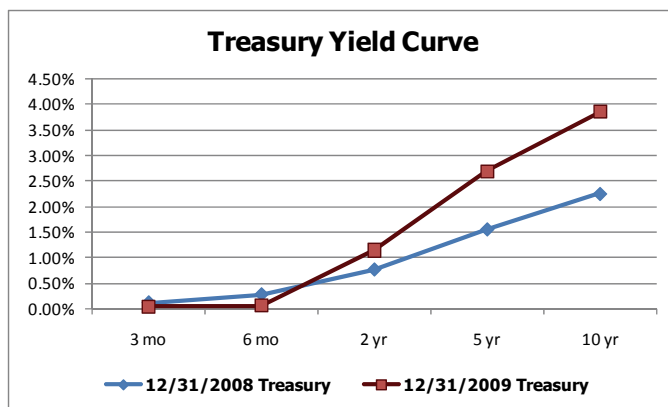
Eastside condominium sales were up 39.8 percent and the median price declined 6.3 percent to \$281,200. Factors for improved sales are attributed to the federal sales tax credit, low interest rates, improving stock market, and more realistic pricing by sellers. While the housing market improved in 2009 compared to 2008, median prices have not returned to the peak reached in 2007. The median price countywide is down about 16.5 percent from 2007.

Seattle metro consumer price index (CPI) peaked at 6.19 percent in June and August 2008. Both the local and national indexes have remained negative or low throughout 2009. The June 2009 CPI (-0.7 percent) is normally used to calculate City employee cost of living adjustments (COLA) for 2010. As a result, employees with closed bargaining units will receive no adjustment in 2010. (Four bargaining units and management had already agreed to this as part of a budget reduction strategy.) The year ended with Seattle CPI at 2.1 percent, which is far below the national city average of 3.4 percent.

Investment Report

MARKET OVERVIEW

Investment earning opportunities continued at all time lows throughout 2009. The Fed Funds rate remained in the range of 0.00 percent to 0.25 percent throughout the year. As can be seen in the accompanying graph, the treasury yield curve has reached new lows on the short end of the curve and steepened some at the longer end of the curve.

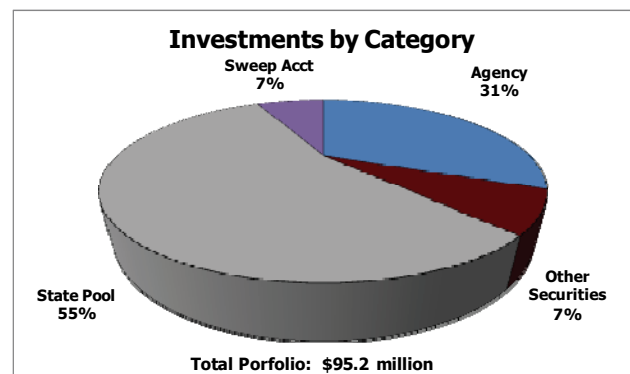


CITY PORTFOLIO

It is the policy of the City of Kirkland to invest public funds in a manner which provides the highest investment return with maximum security while meeting the City's daily cash flow requirements and conforming to all Washington state statutes governing the investment of public funds.

The primary objectives for the City of Kirkland's investment activities are: legality, safety, liquidity and yield. Additionally, the City diversifies its investments according to established

maximum allowable exposure limits so that reliance on any one issuer will not place an undue financial burden on the City. The City's portfolio decreased about \$10 million in 2009. \$5 million of the decrease was due to an equivalent increase to the balance in the City's bank account to increase earnings to offset banking services cost. The remaining \$5 million decrease can be attributed to increased capital expenditures and decreased revenues. On December 31, 2008, Kirkland's portfolio balance was \$105.6 million compared to \$95.2 million on December 31, 2009.



Diversification

The City's current investment portfolio is composed of Government Agency bonds, State and Local Government bonds, the State Investment Pool and an overnight bank sweep account. Kirkland's Investment Policy allows up to 100% of the portfolio to be invested in US Treasuries or US Agency securities, with a limit of 30% of the portfolio invested in any one US Agency.

2009 ECONOMIC OUTLOOK and INVESTMENT STRATEGY

The professional forecasters of the Federal Reserve Bank of Philadelphia expect economic growth of 2.4 percent in 2010 following an approximate 2.5 percent decline in 2009. Core inflation for 2009 is expected to be 1.2 percent. The unemployment rate is expected to average 10 percent for 2010. The Fed Funds rate, currently at 0.00 to 0.25 percent is expected to stay at this level throughout 2010 and possibly through the first half of 2011.

Investment opportunities which provide greater yield are limited during this period of very low interest rates. The goal for 2010 will be to obtain benchmark yields while not investing too far out on the yield curve so that the City will not own a large number of low yield securities when interest rates begin to rise. Total investment income for 2010 is estimated to be \$1.4 million, about half of the interest income for 2009.

Investment Report *continued*

Liquidity

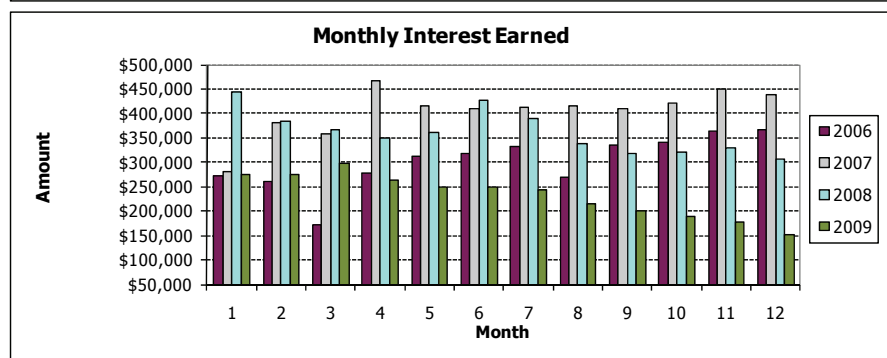
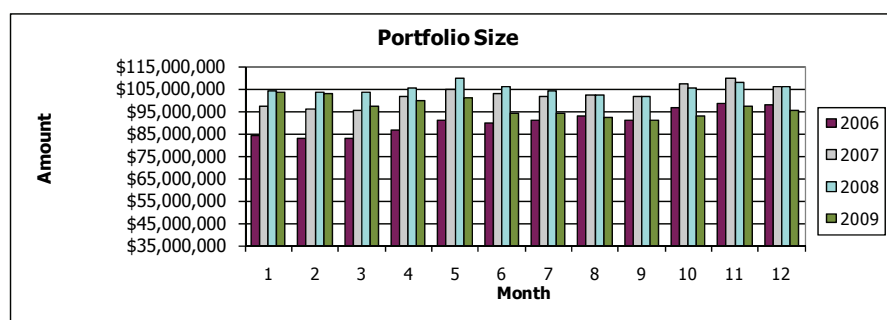
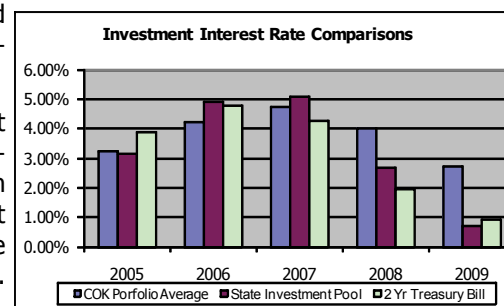
During 2009, the average maturity of the City's investment portfolio decreased from 2.01 years to 0.72 years as many of the securities with callable features were re-deemed. The 2 year treasury rate is used to establish the target duration of the City's portfolio as seen in the table to the right. With the 2 year treasury rate at 1.14% at year end, the target duration is between 0.75 and 1 year. The portfolio at year end was slightly below this as several callable securities were called in the last quarter of 2009.

Benchmark Comparison	December 31, 2008	December 31, 2009
City Yield to Maturity (YTM)	3.57%	1.66%
City Annual Average YTM	4.03%	2.74%
City Year to Date Cash Yield	4.36%	3.04%
State Pool Average Yield	2.68%	0.70%
2 yr Treasury Note Avg YTM	1.97%	0.95%

Yield

The City portfolio yield to maturity decreased from 3.57% on December 31, 2008 to 1.66% on December 31, 2009. Through December 31, 2009, the City's annual average yield to maturity was 2.74%, which significantly outperformed the State Investment Pool annual average yield at 0.70% and as well as the 2 Year Treasury note annual average for 2009 at 0.95%.

The City's practice of investing further out on the yield curve than the State Investment Pool results in earnings higher than the State Pool during declining interest rates and lower earnings than the State Pool during periods of rising interest rates. This can be seen in the adjacent graph.



Reserve Summary

General Operating Reserve

For the City's "Rainy Day" fund, the target is established by fiscal policy at five percent of the operating budget (excluding utility and internal service funds). Each year, the target amount will change proportional to the change in the operating budget. To maintain full funding, the increment between five percent of the previous year's budget and the current budget would be added or subtracted utilizing interest income and year-end transfers from the General Fund. It is a reserve to be used for unforeseen revenue losses and other temporary events. If the reserve is utilized by the City Council, the authorization should be accompanied by a plan for replenishing the reserve within a two to three year period.

Revenue Stabilization Reserve

The Revenue Stabilization Reserve was approved by Council in July 2003 and was created by segregating a portion of the General Operating Reserve. The purpose of this reserve is to provide an easy mechanism to tap reserves to address temporary revenue shortfalls resulting from temporary circumstances (e.g. economic cycles, weather-related fluctuations in revenue). Council set the target at ten percent of selected General Fund revenue sources which are subject to volatility (e.g. sales tax, development fees and utility taxes). The Revenue Stabilization Reserve may be used in its entirety; however, replenishing the reserve will constitute the first priority for use of year-end transfers from the General Fund.

Contingency Fund

The Contingency Fund was established pursuant to RCW 35A.33.145 to "provide monies with which to meet any municipal expense, the necessity or extent of which could not have been foreseen or reasonably evaluated at the time of adopting the annual budget." State law sets the maximum balance in the fund at \$.375 per \$1,000 of assessed valuation. This reserve would be used to address unforeseen expenditures (as opposed to revenue shortfalls addressed by the Revenue Stabilization Reserve). The fund can be replenished through interest earnings up to the maximum balance or through the year-end transfer if needed.

Reserves are an important indicator of the City's fiscal health. They effectively represent "savings accounts" that are established to meet unforeseen budgetary needs (general purpose reserves) or are otherwise dedicated to a specific purpose (special purpose reserves). The City's reserves are listed with their revised estimated balances at the end of the biennium in the table below:

General Government & Utility Reserves Summary

Reserves	2009-10 Est End Balance	2009 Auth. Uses	2009 Auth. Additions	Revised 2009-10 End Balance
GENERAL PURPOSE RESERVES				
Contingency	2,324,515	518,557		1,805,958
General Capital Contingency	2,444,561	266,514		2,178,047
Park & Municipal Reserve:				
General Oper. Reserve (Rainy Day)	2,712,836			2,712,836
Revenue Stabilization Reserve	1,082,380	1,000,000		82,380
Building & Property Reserve	2,059,669	125,000		1,934,669
Council Special Projects Reserve	271,960	104,276		167,684
Total General Purpose Reserves	10,895,921	2,014,347	0	8,881,574
SPECIAL PURPOSE RESERVES				
Excise Tax Capital Improvement:				
REET 1	8,370,417	2,349,314	266,078	6,287,181
REET 2	8,134,095		361,336	8,495,431
Equipment Rental:				
Vehicle Reserve	6,421,787			6,421,787
Radio Reserve	36,000			36,000
Information Technology:				
PC Replacement Reserve	494,373			494,373
Major Systems Replacement Reserve	247,900		197,600	445,500
Facilities Maintenance:				
Operating Reserve	550,000			550,000
Facilities Sinking Fund	1,051,963			1,051,963
Impact Fees				
Roads	3,429,578			3,429,578
Parks	237,809			237,809
Park Bond Reserve	558,981			558,981
Cemetery Improvement	523,405			523,405
Off-Street Parking	204,410			204,410
Tour Dock	70,175			70,175
Street Improvement	994,576			994,576
Firefighter's Pension	1,591,986			1,591,986
Park & Municipal Reserve:				
Litigation Reserve	51,329			51,329
Labor Relations Reserve	67,183			67,183
Police Equipment Reserve	48,093			48,093
LEOFF 1 Police Reserve	612,029			612,029
Facilities Expansion Reserve	800,000			800,000
Development Services Reserve	457,331			457,331
Tree Ordinance	28,980			28,980
Donation Accounts	161,257			161,257
Revolving Accounts	86,175			86,175
Water/Sewer Operating Reserve	1,799,424			1,799,424
Water/Sewer Debt Service Reserve	826,759			826,759
Water/Sewer Capital Contingency	3,018,240	239,200		2,779,040
Water/Sewer Construction Reserve	9,444,066	21,787		9,422,279
Surface Water Operating Reserve	394,485			394,485
Surface Water Capital Contingency	617,690			617,690
Surface Water-Transp. Related Rsv	1,302,179	23,000		1,279,179
Surface Water Construction Reserve	3,186,434			3,186,434
Total Special Purpose Reserves	55,819,109	2,633,301	825,014	54,010,822
Grand Total	66,715,030	4,647,648	825,014	62,892,396

Reserve Summary continued**USES AND ADDITIONS HIGHLIGHTS**

RESERVE	AMOUNT	DESCRIPTION
2009 Council Authorized Uses		
Contingency	\$54,750	Verizon franchise negotiations
	\$188,262	Hydrant Costs
	\$272,000	2009 Firefighter Overtime
	\$3,545	Return 2008 Interest Backfill to General Fund
General Capital Contingency	\$64,000	Downtown Transit Center
	\$43,800	NE 73rd Street Sidewalk additional funding
	\$98,544	Return 2008 Interest Backfill to General Fund
	\$60,170	Pandemic Flu Supplies
Revenue Stabilization Reserve	\$1,000,000	Backfill General Fund revenue deficit
Building & Property Reserve	\$125,000	Return 2008 Interest Backfill to General Fund
Council Special Projects Reserve	\$2,000	Council Retreat facilitator
	\$26,000	Funding for federal lobbyist services for 2009.
	\$25,000	Funding for Neighborhood Connections in 2010.
	\$20,000	Hopelink relocation
	\$13,770	Flexpass program
	\$12,506	Bank of America project review process
	\$5,000	Council special investigation
Excise Tax Capital REET 1	\$2,349,314	Municipal Court Building purchase
Water/Sewer Capital Contingency	\$54,000	Additional funding of \$54,000 for telemetry system upgrades at Supply Station #2 to coincide with a City-wide upgrade of telemetry panels at other water facility sites.
	\$128,000	Funding for the completion of the 2009 Water System Improvement Project.
	\$17,200	NE 73rd Street Sidewalk (watermain replacement) additional funding
	\$40,000	3rd Street Watermain Replacement
Water/Sewer Construction Reserve	\$21,787	Bridle View Annexation Water System Purchase from Redmond
Surface Water-Transp. Related Rsv	\$23,000	Downtown Transit Center (surface water component)
2009 Council Authorized Additions		
Excise Tax Capital REET 1	\$266,078	Closed Capital Projects
Excise Tax Capital REET 2	\$361,336	Closed Capital Projects
Major Systems Replacement Reserve	\$197,600	Closed Capital Projects

General Government & Utility Reserves Targets Summary

Reserves	Revised 2009-10 End Balance	2009-10 Target	Over (Under) Target
GENERAL PURPOSE RESERVES			
Contingency	1,751,208	4,915,571	(3,164,363)
General Capital Contingency	2,178,047	9,032,430	(6,854,383)
Park & Municipal Reserve:			
General Oper. Reserve (Rainy Day)	2,712,836	3,567,649	(854,813)
Revenue Stabilization Reserve	82,380	2,188,803	(2,106,423)
Council Special Projects Reserve	167,684	250,000	(82,316)
General Purpose Reserves with Targets	6,892,155	19,954,453	(13,062,298)
SPECIAL PURPOSE RESERVES			
Excise Tax Capital Improvement:			
REET 1	6,287,181	1,653,500	4,633,681
REET 2	8,495,431	8,477,130	18,301
Firefighter's Pension	1,591,986	1,103,000	488,986
Park & Municipal Reserve:			
Litigation Reserve	51,329	50,000	1,329
Water/Sewer Operating Reserve	1,799,424	1,799,424	0
Water/Sewer Debt Service Reserve	826,759	826,759	0
Water/Sewer Capital Contingency	2,779,040	3,018,240	(239,200)
Surface Water Operating Reserve	394,485	394,485	0
Surface Water Capital Contingency	617,690	617,690	0
Special Purpose Reserves with Targets	22,843,325	17,940,228	4,903,097
Reserves without Targets	33,102,166	n/a	n/a
Total Reserves	62,837,646	n/a	n/a

The summary above details all Council authorized uses and additions to each reserve through December 2009.

An additional transfer of \$1 million from the Revenue Stabilization Reserve was approved with mid-year budget adjustments, which effectively uses up this reserve as a resource.

The table to the left compares the revised ending balance to the targets established in the budget process for those reserves with targets.



123 5th Avenue
Kirkland, Washington 98033
425-587-3101

- ◆ Tracey Dunlap, Director of Finance & Administration
- ◆ Michael Olson, Deputy Director of Finance & Administration
- ◆ Sandi Hines, Financial Planning Manager
- ◆ Sri Krishnan, Senior Financial Analyst
- ◆ Neil Kruse, Budget Analyst
- ◆ Tammy McCorkle, Budget Analyst

www.ci.kirkland.wa.us

The Financial Management Report (FMR) is a high-level status report on the City's financial condition that is produced quarterly.

- It provides a **summary budget to actual comparison** for year-to-date revenues and expenditures for all operating funds. The report also compares this year's actual revenue and expenditure performance to the prior year.
- The **Sales Tax Revenue Analysis** report takes a closer look at the City's largest and most economically sensitive revenue source.
- **Economic environment** information provides a brief outlook at the key economic indicators for the Eastside and Kirkland such as office vacancies, residential housing prices/sales, development activity, inflation and unemployment.
- The **Investment Summary** report includes a brief market overview, a snapshot of the City's investment portfolio, and the City's year-to-date investment performance.
- The **Reserve Summary** report highlights the uses of and additions to the City's reserves in the current year as well as the projected ending reserve balance relative to each reserve's target amount.

Economic Environment Update References:

- *NW purchasing managers' optimism drops in November*, Puget Sound Business Journal, December 7, 2009
- *U.S. consumer confidence index 52.9 in December*, Reuters, December 29, 2009
- Eric Pryne, *Home sales on King County's Eastside lead December activity*, The Seattle Times, January 6, 2010
- *Washington State's Recovery: U Shaped?*, The Puget Sound Business Journal, January 29, 2010
- *A rooftop view of 2009*, The Seattle Times, February 7, 2010
- CB Richard Ellis Real Estate Services, Market View Puget Sound, Fourth Quarter 2009
- U.S. Bureau of Labor Statistics
- Washington State Economic & Revenue Forecast Council
- Washington State Employment Security Department
- Washington State Department of Revenue
- Washington State Department of Labor & Industries
- City of Kirkland Building Division
- City of Kirkland Finance Department